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SIPDIS

SENSITIVE, SIPDIS

DOL/ILAB FOR TINA MCCARTER

DRL/IL FOR LAUREN HOLT

STATE FOR SA/INS

MCC FOR D NASSIRY AND E BURKE

GENEVA PASS USTR

DEPARTMENT PASS TO US TRADE REPRESENTATIVE
USTR FOR K BHATIA AND D HARTWICK

E.O 12958: N/A

TAGS: [ECON](#) [ELAB](#) [EIND](#) [ETRD](#) [EAID](#) [CE](#)

SUBJECT: 5TH ROUND OF TIFA TALKS HIGHLIGHT ON OBSTACLES TO US
INVESTMENT

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This message is sensitive but unclassified.

11. (SBU) Summary. The Office of the US Trade Representative and the Sri Lankan Ministry of Trade, Commerce, Consumer Affairs and Marketing Development held the Fifth Joint Council Meeting under the bilateral US-Sri Lanka Trade and Investment Framework Agreement (TIFA) in Colombo on December 1. Minister Jeyaraj Fernandopulle raised the importance of apparel to Sri Lanka's exports and noted the recent challenges affecting Sri Lanka's economy including the 2004 tsunami, the high price of oil in the past year, and the increase of global competition in key industries. The U.S. delegation stressed the importance of pursuing sound macro-economic, tariff, intellectual property and investment policies. The two sides discussed how Sri Lanka can make effective use of US trade capacity building programs. Both sides expressed the desire to see a successful and ambitious outcome to the Doha Round of trade negotiations. End Summary.

12. (SBU) DUSTR Karan Bhatia, AUSTR Douglas Hartwick, AUSTR Mary Ryckman, USTR Special Assistants Manpreet Anand and Neil Herrington, Intellectual Property Officer Dominic Keating, and Agricultural Attache to New Delhi Gerald Smith, accompanied by Ambassador Robert 10. Blake and Econoffs, attended the fifth round of US-Sri Lanka TIFA talks held in Colombo on December 1. Jeyaraj Fernandopulle, Minister of Trade, Commerce, Consumer Affairs and Marketing Development, led the Sri Lankan delegation.

Trade Liberalization Status

13. (SBU) Minister Fernandopulle opened the talks by commenting on his desire to recommence discussions for a Free Trade Agreement (FTA) between the U.S. and Sri Lanka, noting the positive movements made in this direction under the previous government. The Minister went on to note how Sri Lanka has embarked on trade liberalizing policies with other countries, including an FTA with Pakistan in 2005, a bilateral investment agreement with India, and participation in the South Asia Free Trade Agreement (SAFTA). Ambassador Bhatia responded that while it is not likely that FTA discussions could commence soon, continued trade liberalization policies are necessary precursors to future FTA negotiations.

14. (SBU) Minister Fernandopulle also explained that, despite economic growth of 7%, Sri Lanka faces several economic challenges including high fuel costs, recovering from the tsunami, adjusting to tougher global competition, and the ongoing conflict. The Minister emphasized that Sri Lanka was one of the first countries to liberalize trade in South Asia and that Sri Lanka's current liberalization commitments are reflected in various bilateral and regional free trade agreements. However, the Sri Lankan economy is still largely based on agriculture, making agricultural liberalization difficult. Sri Lanka is seeking protection under the special products mechanism for agricultural products that it produces locally. Ambassador Bhatia noted that there is a cost to Sri Lanka's economic future in staying agriculturally-based as opposed to moving towards industrialization, especially in terms of subsidies.

15. (SBU) Ambassador Bhatia spoke briefly about Sri Lanka's import tariff regime, noting that investment can be stymied with large import tariff structures. Ambassador Bhatia said that it seemed a significant amount of Sri Lanka's revenues came from import tariffs, which can make liberalization reforms politically difficult. The Sri Lanka delegation responded that in the next ten years, Sri Lanka will continue moving substantially towards a tax structure, rather than an import tariff regime for its revenue.

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The Doha Development Round

16. (SBU) Ambassador Bhatia stressed the importance of the Doha round and U.S. commitment to the Doha Development Agenda. He noted that the U.S. wants to reduce tariffs as well as domestic subsidies and that the Doha round should be a collective effort of countries around the world, not just the U.S. and the EU. Minister Fernandopulle confirmed that Sri Lanka will support the U.S. on Doha. However, as a net food importer, Sri Lanka is concerned that a reduction of agricultural subsidies would increase import prices. Sri Lanka is also seeking increased market access for professional services, industrial products, and particularly for garments.

Securing Greater Market Access to the U.S.

17. (SBU) The Sri Lankan delegation made their case for preferential tariffs for apparel exported to U.S. and highlighted Sri Lanka's positive record of labor standards and welfare. They pointed out that some of Sri Lanka's competitors have free or preferential access to U.S. Sri Lanka seeks support through the extension of benefits granted to least-developed countries (LDCs) and hopes that the U.S. will consider Sri Lanka's vulnerability and extend these benefits.

18. (SBU) Ambassador Bhatia had a pre-TIFA briefing with the Joint Apparel Association Forum (JAAF) on this same topic. Sri Lanka's apparel exports to the U.S. have declined 1% in the first 9 months of 2006. JAAF participants said they faced severe price competition from China which could disrupt the apparel industry; especially the smaller factories. They stressed the importance of a stable garment industry for Sri Lanka's political stability and economic development. JAAF also said that once peace returns, the garment industry could be a catalyst for growth in the North and East. JAAF

has already embarked on a program to showcase Sri Lanka's strong adherence to international labor standards. JAAF requested that concessions be granted at least for apparel made with US yarn or fabric. Ambassador Bhatia stressed that market based principles are the way to move forward in apparel and suggested that Sri Lanka undertake a trip to the U.S. to showcase the good work they are doing in the apparel sector.

National Drug Policy

¶9. (SBU) Sri Lanka imports USD 20 million worth of pharmaceutical items from the US. These U.S. exports could be negatively impacted if certain clauses of the National Drug Policy (NDP) are implemented. Sri Lankan Ministry of Health officials stated that the current procurement procedure is based on competitive prices and WHO recommendations. The Health Ministry buys largely from known suppliers and decides on quality and quantity. The GSL is committed to providing free health care to the population, especially in the face of changing demographics and increasingly prevalent terminal illnesses. Importers registered with the Ministry of Health can have free access to the local market. A panel will determine what drugs Sri Lanka requires. However, this does not mean that other drugs cannot be imported. Users can also import on user license, the GSL will continue to procure drugs recommended by WHO, and private sector health providers can import drugs once they are registered. The NDP's purpose is to prevent unwanted drugs coming in. Ambassador Bhatia suggested a digital video conference between the two sides on this issue and the GSL agreed to look into setting up a working committee on the NDP.

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GMO Food Certification

¶10. (SBU) The USG sees Sri Lanka's proposed GMO food labeling requirements as a non-tariff barrier and has provided comments on the draft legislation that will be tabled at the next Food Advisory Committee meeting. According to the USDA, the draft regulation has inconsistencies and is not based on scientific justification. Dr. Shanmugarajah of the Sri Lankan Health Ministry said Sri Lanka was obliged to develop a GM regulation as a signatory to the Cartagena Protocol, that certain consumer groups were lobbying for the regulation, and that there is a Supreme Court order to expedite the labeling regulation. He explained that the regulation is not a ban and that its purpose is to regulate the import of GMOs into the country. An expert committee will be set up to recommend approval or rejection of the products on a case by case basis. There is no capacity in Sri Lanka for risk analysis, so the Health Ministry will review certificates of food from other countries (eg. USDA). The onus of responsibility will lie with the importer to prove that the food is safe and a transition period will be allowed when the regulations come into effect. Dr. Ratnayake of the Ministry of Trade reassured the US delegation that these regulations would not become a barrier. The GSL agreed to nominate the Director General for Department of Commerce as a POC on this issue.

Seed Potatoes

¶11. (SBU) On the seed potatoes issue, FAS New Delhi pointed out that the United States is actively working with the GSL officials to provide market access for U.S. seed potatoes. The United States Department of Agriculture (USDA) and the Sri Lankan Department of Agriculture (DOA) are currently in technical discussion to resolve this issue. FAS New Delhi informed the meeting that as of November 14, 2006 the Director General of Agriculture permitted the importation of seed potatoes subject to two requirements. FAS New Delhi informed the Sri Lankan side that a formal technical letter from APHIS/PPQ with further details regarding our position on the above referenced requirements is forthcoming. The USG suggested that this would require more discussion between APHIS and the

The Current Investment Climate

¶12. (SBU) The Sri Lanka Board of Investment gave a presentation on the current investment climate, stressing reforms in their government procurement policies.

¶13. (SBU) Ambassador Hartwick pointed out that the trade balance, surprisingly, is 10 to 1 in favor of Sri Lanka. The U.S. delegation raised the issues of high tariffs, creeping cesses, and other duties on imports. The GSL explained that there are low tariffs for inputs, machinery and intermediate goods, and high tariffs for finished goods. Sri Lanka is dependent on tariffs of finished goods as most goods fall under categories with low duties. Intermediate goods account for 62% of imports, food accounts for 17%, and finished products 20%. Recent FTAs and regional trading agreements have eroded the border tariffs, which are an important source of income and account for 12% of revenue. Until domestic revenue is more broadly based, they will not be able to reduce the border tariffs. The Sri Lankan delegation offered to consider reducing tariffs on items of interest to US exporters on a product by product and case by case basis. Ambassador Bhatia suggested that

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they look at reducing tariffs on a sector by sector basis.

¶14. (SBU) Ambassador Bhatia said he would like to see more US investments in Sri Lanka and trade promotion elements in projects promoted by the MCC. He said roads, training and SME development could all have a high component of trade promotion.

¶15. (SBU) The GSL is looking for foreign investment in infrastructure and in backward integration in the textile industry. The Board of Investment (BOI) is in a position to grant incentives in those areas, and the FTAs with India and Pakistan make Sri Lanka an attractive location for foreign investors who are interested in exporting to those countries. Sri Lanka has the highest market access (4,500 items duty free) to India in the region. The BOI identified automobile and electrical components as two possible intermediate products that can be made in Sri Lanka. Sri Lanka also hopes to develop an IT industry with links to South India. Ambassador Bhatia suggested that Sri Lanka may have to target companies looking at India and convince them to come to Sri Lanka.

Transparency in Government Procurement

¶16. (SBU) Sri Lankan government procurement totals USD 1 billion per year. President Rajapaksa has stressed the need for transparency in government procurement and the GSL has drawn up procurement guidelines to increase transparency. According to Dr. D.M. Karunaratne, Director General of the National Procurement Agency (NPA), each Technical Evaluation Officer in the Technical Evaluation Committee (TEC) has individual responsibility for certain aspects of the tender review process. Most malpractice in procurement takes place when urgent procurements are requested. The Treasury will not fund procurement unless a procurement plan is prepared. Bidding documents are prepared in line with similar documents of funding agencies. If specifications are biased, the TEC has to re-examine the tender. Specifications of bidding documents have to be of a generic nature and reflect functional aspects. Several improvements have been made to the tender guidelines, according to Karunaratne. Bidders also have the opportunity to protest if the specifications are biased. Post procurement auditing does not take place.

Contract Sanctity

¶17. (SBU) Ambassador Hartwick raised the issue with Jacobi Carbons, indicating that this kind of case sends a bad signal to potential

investors to Sri Lanka. The GSL responded that the Gazette notification that effectively restricted Jacobi Carbons from obtaining local raw material was not made with the concurrence of Minister Fernandopulle, which was required. The cabinet has reviewed the issue and determined that the local material restriction was incorrect and would be removed. The court was to be advised of this determination. As such, the Chief Justice's order for a settlement was no longer valid. This determination was being conveyed to Jacobi Carbons.

IPR Enforcement and Technical Assistance

¶18. (SBU) Dominic Keating, US PTO officer from Delhi, stressed the importance of effective enforcement of the 2003 intellectual property law in order to enhance investment in Sri Lanka. Keating encouraged the GSL to ratify and implement the World Intellectual Property Organization (WIPO) Copyright Treaty (WCT) and the WIPO

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Performances and Phonograms Treaty (WPPT). Keating also requested an update on the implementation of the GSL 2003 IPR law.

¶19. (SBU) Karunaratne reported that Sri Lanka is discussing with the World Intellectual Property Organization (WIPO) the development of a national strategy on IPR (NSIPR). He hopes to initiate work on the NSIPR in 2007. The strategy will encompass IP norms, implementation, enforcement, public awareness, and using IP for economic development. A new customs implementing regulation will be published soon which will improve customs enforcement. The IPR office will also be automated. Some classes of trademarks require a long period for registration, some as long as 1 to 2 years, but there is no back-log on patents and designs. The IP office also acts as a mediator in disputes involving copy rights and related rights. Ambassador Bhatia suggested that someone from the GSL meet with Jon Dudas, the Department of Commerce Under Secretary for Intellectual Property and Director of the Patent and Trademark Office, when he visits India in mid-December.

¶20. (SBU) The GSL requested assistance in developing a database to find the owners of trademarks and in human resource development and training. Keating responded that he would take these requests back to the relevant USG officials.

GSP Status and Diversification

¶21. (SBU) Ambassador Bhatia discussed the GSP program and the upcoming re-authorization. He informed the Sri Lankan delegation that GSP now accepts SAARC accumulation for rules of origin purposes. Sri Lanka's GSP utilization rate is about 88% and in line with the global average.

¶22. (SBU) The GSL requested that products exported to the US but made with yarn imported from the US be eligible for duty-free treatment. Ambassador Bhatia acknowledged the rationale behind this request and said that the USG would respond on this issue.

Millennium Challenge Corporation

¶23. (SBU) The discussion on the MCC was held over lunch with the new lead for GSL's MCC team, Dhara Wijayatilake. She is well-versed in the current proposal and aware that the MCC has decided not to invest in the large irrigation project, including four dams, that was part of the initial GSL's proposal. The GSL understands the reasons why the MCC took this decision, as extensive due diligence remains to be done on environmental impact assessments and related issues. The GSL is likely to press ahead with the remaining elements of the initial proposal, but would like to discuss with the MCC if it would be possible to include an investment in an existing information technology program which aims to bring technology to the rural schools. Ms. Wijayatilake would like to have this considered,

but does not want to cause extensive delay in completing the MCC compact.

Trade Capacity Building

¶24. (SBU) Sonali Wijeratne of the Department of Commerce explained various programs Sri Lanka has undertaken to build awareness of the benefits of global trade. Sri Lanka has recently established a trade remedy unit which works on anti-dumping and counter-vailing duties legislation, and requested assistance to do this. Ryckman noted that the US Department of Commerce has conducted some training

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in this area to help countries set up WTO-consistent trade rules. The GSL also would like additional training in international trade law. The US suggested this might be an area where the WTO-provided assistance could help. Finally, the GSL provided a paper on a request to expand IT capabilities of the government to better connect its offices overseas, including its 23 offices that are responsible for the promotion of Sri Lanka's economic and trade interests. The USG said it would take the proposal back to capital to for consideration.

¶25. (SBU) Comment: Sri Lanka's proposed GMO regulation, the NDP and government procurement practices could have adverse effects on U.S. trade to Sri Lanka unless these issues are addressed in a meaningful manner. Despite reassurances from the GSL, if the NDP and GMO regulations are implemented in their current form we expect that there will be a negative impact on U.S. exports. Heavy political influence continues to prevent procurement systems from being effective, a problem that is reflected in Sri Lanka's slide on Transparency International's corruption perception index from 78 in 2005 to 84 in 2006. For the Sri Lankan side, the most critical issue with regard to bilateral trade remains seeking preferred U.S. market access for apparel through an FTA or other trade preference vehicles.

BLAKE